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Before the  
Federal Communications Commission  
Washington, D.C. 20554

CC Docket No. 96-22

In the Matters of

Responsible Accounting Officer                      AAD 92-65  
Letter 20, Uniform Accounting for  
Postretirement Benefits Other  
Than Pensions in Part 32

Amendments to Part 65, Interstate Rate  
of Return Prescription Procedures and  
Methodologies, Subpart G, Rate Base

# MEMORANDUM OPINION AND ORDER AND NOTICE OF PROPOSED RULEMAKING

Adopted: February 20, 1996;                      Released: March 7, 1996

By the Commission:

Comment Date: April 12, 1996

Reply Comment Date: May 14, 1996

## I. INTRODUCTION

1. On June 3, 1992, the Ameritech Operating Companies (Ameritech) and the Bell Atlantic Telephone Companies (Bell Atlantic) filed Applications for Review of Responsible Accounting Officer Letter No. 20 (RAO 20).<sup>1</sup> The Common Carrier Bureau (Bureau) issued that letter on May 4, 1992, to provide accounting and ratemaking instructions to carriers for postretirement benefits other than pensions (OPEB).<sup>2</sup> Ameritech and Bell Atlantic claim that the Bureau's instructions contradict the Commission's accounting and rate base rules,<sup>3</sup> and that the Bureau therefore exceeded its delegated authority in issuing those instructions.<sup>4</sup> For the reasons discussed below,<sup>5</sup> we affirm the accounting instructions, but vacate the ratemaking instruc-

tions. We also adopt a Notice of Proposed Rulemaking that proposes amendments to Part 65, Subpart G of our rules, which would revise the rate base treatment of postretirement benefits other than pensions.<sup>6</sup>

## II. BACKGROUND

2. Since 1935, the Commission has used accounting interpretations to give regulatory accounting guidance to telephone companies. Initially, the vehicles for delivering these interpretations were case studies issued in response to questions carriers had submitted.<sup>7</sup> In 1987, the vehicle became Responsible Accounting Officer (RAO) Letters.<sup>8</sup> Under Section 32.17 of our rules,<sup>9</sup> these letters are issued to maintain uniformity within the system of accounts prescribed in our Part 32 rules. Generally, the Bureau issues these letters to provide guidance to carriers in response to accounting questions. The letters' purpose is to explain, interpret, or resolve accounting matters.<sup>10</sup>

3. The Bureau issued RAO 20 primarily to provide guidance to carriers on how to account for OPEB costs in a manner consistent with Statement of Financial Accounting Standards No. 106 (SFAS-106), Employers' Accounting for Postretirement Benefits Other Than Pensions, which the Financial Accounting Standards Board (FASB) adopted in December 1990.<sup>11</sup> SFAS-106 established new financial accounting and reporting requirements for employers offering postretirement benefits other than pensions to employees. To be in conformance with generally accepted accounting principles (GAAP), companies were required to follow these new requirements for accounting periods beginning after December 15, 1992.

4. Before SFAS-106, GAAP required companies to account for OPEB costs on a cash basis. This meant that companies recognized the OPEB amounts actually paid on behalf of employees in the accounting period when the payments were made. SFAS-106 required companies to account for OPEB costs on an accrual basis, treating OPEB costs as a form of deferred compensation that employees earn during their working years. As a result, to comply with GAAP, companies had to recognize OPEB costs as expenses during the years the benefits are earned and to record a liability for benefit amounts owed to employees.

5. The change from cash-based to accrual accounting requires each company to recognize on its books of account the amount of its OPEB obligation to retirees and to active employees that existed as of the date the company

<sup>1</sup> Uniform Accounting for Postretirement Benefits Other Than Pensions in Part 32, 7 FCC Rcd 2872 (Com. Car. Bur. 1992) (RAO 20).

<sup>2</sup> OPEBs are all forms of benefits, other than retirement income, provided by an employer to retirees. Those costs typically consist of health and dental care benefits and life insurance premiums of retired employees.

<sup>3</sup> The accounting rules are codified at 47 C.F.R. Part 32. The rate base rules, codified at 47 C.F.R. §§65.800-830, list the Part 32 accounts that are to be included in and excluded from the rate base that telephone companies use to calculate their interstate costs. Generally, the interstate rate base consists of amounts that are prudently invested in plant that is used and useful in the provision of interstate telecommunications services.

<sup>4</sup> GTE Service Corporation (GTE), New York Telephone Company and New England Telephone and Telegraph Company (NYNEX), Pacific Bell and Nevada Bell (Pacific Telesis) and the

Washington Utilities and Transportation Commission (WUTC) filed comments on the Applications for Review. Ameritech and Bell Atlantic filed replies.

<sup>5</sup> See discussion *infra* part III.

<sup>6</sup> See *infra* part V.

<sup>7</sup> See 47 C.F.R. Part 31, Appendix A (1987) (setting forth over 20 accounting interpretations issued between December 11, 1935 and December 27, 1963).

<sup>8</sup> In Responsible Accounting Officer Letter No. 5, released on April 15, 1987, the Bureau informed carriers that henceforth RAO Letters would be the medium through which the Bureau would respond to requests for interpretations of the Commission's accounting rules.

<sup>9</sup> 47 C.F.R. §32.17.

<sup>10</sup> See *id.*

<sup>11</sup> The FASB is the authoritative standard setting body for accounting practices that are used in the American business community.

adopted SFAS-106. This obligation equals the amount that the company would have accrued on its books as of the effective date of the accounting change if it had been operating under the accrual method and is referred to as the "transitional benefit obligation." SFAS-106 permits companies either to charge their transitional benefit obligations to expense and record the full liability immediately, or to amortize the transitional benefit obligations and accrue the liabilities over the average remaining service periods of current employees. If the average remaining service period is less than 20 years, the employer may elect to use a 20-year period.

6. Since 1985, the Commission has followed a policy of conforming regulatory accounting for carriers to GAAP, including new FASB standards, unless the principle or practice conflicts with the Commission's regulatory objectives.<sup>12</sup> In December 1991, the Bureau issued an Order authorizing telephone companies to adopt SFAS-106 type accounting for OPEB costs, on or before January 1, 1993.<sup>13</sup> The Bureau declined, however, to allow carriers to adopt the FASB option of immediately recognizing their transitional benefit obligations, because the amounts involved were so large that booking them as one-time expenses would have distorted the carriers' earnings during the affected period. Instead, the Bureau authorized the carriers to use the other SFAS-106 option of amortizing transitional benefit obligation expenses either over the average remaining service period of active plan participants or over a 20-year period.<sup>14</sup>

7. On May 4, 1992, the Bureau released RAO 20 in order to tell carriers which Part 32 accounts should be used to record OPEB costs under SFAS-106. RAO 20 also addressed the regulatory treatment of the transitional benefit obligation. Under RAO 20, the transition benefit obligation was to be amortized over the same time period as allowed in SFAS-106 for financial reporting purposes. RAO 20 also clarified that carriers with fewer than 500 employees would not be required to adopt SFAS-106 until

1995. Furthermore, RAO 20 instructed each carrier to notify the Commission within thirty days of the date that carrier adopts SFAS-106 for regulatory accounting purposes. Finally, RAO 20 directed the carriers to exclude accrued OPEB liability from their interstate rate base and to include prepaid OPEB benefits in their interstate rate base.<sup>15</sup>

8. After adopting SFAS-106 for regulatory purposes, several local exchange carriers (LECs) subject to price cap regulation filed tariff transmittals that sought exogenous treatment of the increase in OPEB costs resulting from the accounting change required under SFAS-106.<sup>16</sup> The Bureau suspended these transmittals for five months and set them for investigation.<sup>17</sup> On January 22, 1993, the Commission adopted an Order terminating the investigation and denying the LECs' requests for exogenous treatment of OPEB costs.<sup>18</sup> The price cap LECs sought review of this Order in the United States Court of Appeals for the District of Columbia Circuit. On July 12, 1994, the Court reversed and remanded the Commission Order, finding that the basis of the Commission's decision to deny exogenous cost treatment for OPEB cost changes was not contemplated by the price cap rules.<sup>19</sup>

9. After the Commission Order disallowing ongoing OPEB costs, several LECs filed tariffs to adjust their price cap indices to include transition benefit obligation amounts. The Bureau suspended these tariffs for one day and set them for investigation.<sup>20</sup> AT&T also amended its price cap indices to include the changes in its costs due to the LEC OPEB amounts and added its own transition benefit obligation amounts. These AT&T tariffs were similarly suspended and included in the LECH investigation.<sup>21</sup> After the Court's reversal of the Commission Order, several LECs filed tariff revisions to adjust their price cap indices to include their ongoing OPEB costs. The Bureau suspended these tariffs for one day and initiated investigations.<sup>22</sup> All of these investigations are pending.<sup>23</sup> In addition, in its subsequent review of price cap rules governing

<sup>12</sup> See Revision of the Uniform System of Accounts for Telephone Companies to Accommodate Generally Accepted Accounting Principles, *Report and Order*, 102 FCC 2d 964 (1985); 47 C.F.R. §32.16.

<sup>13</sup> See Southwestern Bell, GTE Service Corporation, Notification of Intent To Adopt Statement of Financial Accounting Standards No. 106, Employers' Accounting for Postretirement Benefits Other Than Pensions, *Order*, 6 FCC Rcd 7560 (Com. Car. Bur. 1991) (*Adoption Order*).

<sup>14</sup> *Id.*

<sup>15</sup> RAO 20, *supra* note 1, at 2872-73.

<sup>16</sup> See Bell Atlantic Telephone Companies, Tariff F.C.C. No. 1, Transmittal No. 497 (filed Feb. 28, 1992); US West Communications, Inc., Tariff F.C.C. Nos. 1 and 4, Transmittal No. 246 (filed Apr. 3, 1992); Pacific Bell Tariff F.C.C. No. 128, Transmittal No. 1579 (filed Apr. 16, 1992). Exogenous treatment has the practical effects of changing the rates interexchange carriers pay LECs for access to local telephone networks and, if interexchange carriers pass the cost changes through to their customers, of changing the rates consumers pay for interstate telephone services.

<sup>17</sup> Treatment of Local Exchange Carrier Tariffs Implementing Statement of Financial Accounting Standards, "Employers' Accounting for Postretirement Benefits Other Than Pensions," Bell Atlantic Tariff F.C.C. No. 1, US West Communications, Inc. Tariff F.C.C. Nos. 1 and 4, Pacific Bell Tariff F.C.C. No. 128, *Order of Investigation and Suspension*, 7 FCC Rcd 2724 (Com. Car. Bur. 1992) (*Investigation Order*).

<sup>18</sup> Treatment of Local Exchange Carrier Tariffs Implementing

Statement of Financial Accounting Standards, "Employers' Accounting for Postretirement Benefits Other Than Pensions," Bell Atlantic Tariff F.C.C. No. 1, US West Communications, Inc. Tariff F.C.C. Nos. 1 and 4, Pacific Bell Tariff F.C.C. No. 128, *Memorandum Opinion and Order*, 8 FCC Rcd 1024 (1993) (*OPEB Order*). Under the definition in effect in 1993, exogenous costs were changes in costs triggered by administrative, legislative, or judicial action that are beyond the control of the carriers. Exogenous costs result in an adjustment to a carrier's price cap index (PCI) to ensure that the price cap formula does not lead to unreasonably high or low rates as a result of these cost changes.

<sup>19</sup> *Southwestern Bell Tel. Co. v. FCC*, 28 F.3d 165, 169-71 (D.C. Cir. 1994).

<sup>20</sup> 1993 Annual Access Tariff Filings, National Exchange Carrier Association, Universal Service Fund and Lifeline Assistance Rates, GSF Order Compliance Filings, Bell Operating Companies Tariffs for the 800 Service Management System and 800 Data Base Access Tariffs, *Memorandum Opinion and Order Suspending Rates and Designating Issues for Investigation*, 8 FCC Rcd 4960 (Com. Car. Bur. 1993) (*1993 Annual Access Investigation Order*).

<sup>21</sup> AT&T Communications Tariff F.C.C. Nos. 1 and 2, Transmittal Nos. 5460, 5461, 5462 and 5464, *Memorandum Opinion and Order Suspending Rates and Designating Issues for Investigation*, 8 FCC Rcd 6227 (Com. Car. Bur. 1993) (*AT&T OPEB Investigation Order*).

<sup>22</sup> Bell Atlantic Telephone Companies Tariff F.C.C. No. 1, Transmittal No. 690, NYNEX Telephone Companies Tariff

LECs the Commission decided that henceforth all OPEB costs should be considered exogenous only to the extent they represent economic cost changes.<sup>24</sup>

10. On July 21, 1995, the Bureau released the 1995 Annual Access Order for price cap LECs.<sup>25</sup> This Order required those LECs that had not already done so to remove all OPEB costs from their 1995 interstate access rates. Subsequently, on July 27, 1995, the Bureau released an Order requiring the NYNEX Telephone Companies (NYNEX) and Pacific Bell to remove from their 1995 interstate access rates all OPEB-related costs that those companies had incurred in 1993 and 1994.<sup>26</sup> This Order also suspended for one day tariff revisions NYNEX and Pacific Bell had filed to recover those specific OPEB costs and incorporated those tariffs into its ongoing investigation of NYNEX's and Pacific Bell's proposals for exogenous treatment of OPEB costs.<sup>27</sup>

### III. DISCUSSION

#### A. RAO 20 Accounting

##### 1. Instructions

11. RAO 20 instructed carriers to use Account 4310, Other Long-Term Liabilities, to record the accrued liability related to OPEBs; Account 1410, Other Noncurrent Assets, to record any OPEB prepayments; and the Part 32 expense accounts to record the current year net periodic OPEB costs,<sup>28</sup> disaggregated into subsidiary categories as required by the expense matrix in Section 32.5999(f) of our rules.<sup>29</sup> The expense matrix disaggregates the Part 32 expense accounts into five categories: salaries and wages; benefits; rents; other expenses; and clearances.<sup>30</sup> The benefits category was designed to include payroll-related benefits such as pensions, saving plan contributions, worker's compensation, life, hospital, medical, dental and vision plan insurance, and social security and other payroll taxes.<sup>31</sup> Finally,

RAO 20 instructed each carrier to continue to use Account 6728, Other General and Administrative, to record payments to retired employees until the carrier actually adopts SFAS-106 accounting.

##### 2. Pleadings

12. Bell Atlantic argues that RAO 20 changed the Commission's accounting rules and is therefore beyond the scope of the Bureau's delegated authority.<sup>32</sup> Bell Atlantic states that Section 32.6728 of the rules<sup>33</sup> requires payments to retirees to be recorded in Account 6728, Other General and Administrative, and that RAO 20 changed this rule by directing carriers to distribute OPEB costs among the expense accounts in accordance with the expense matrix in Section 32.5999(f).<sup>34</sup>

13. GTE and Pacific Telesis also claim that RAO 20 improperly changed the accounting rules.<sup>35</sup> Pacific Telesis argues that adoption of these changes without notice and comment violated Section 553 of the Administrative Procedures Act.<sup>36</sup> GTE states that it included specific language to revise Part 32 in its notice of intent to adopt SFAS-106. GTE continues to recommend that language and suggests that the Commission issue a Notice of Proposed Rulemaking concerning accounting for OPEB costs.<sup>37</sup>

14. NYNEX disagrees with the Bell Atlantic and Pacific Telesis. NYNEX states that RAO 20 did not change Part 32 and that Part 32 was designed to incorporate GAAP changes like SFAS-106 that the Commission accepts in light of regulatory considerations.<sup>38</sup> While NYNEX acknowledges that minor language changes to Account 6728 to implement SFAS-106 would be helpful, NYNEX states that a separate rulemaking proceeding is not needed to accomplish such an administrative detail.<sup>39</sup>

##### 3. Decision

15. After considering the parties' arguments, we find that the directions given in RAO 20 concerning the accounting treatment of OPEB costs were correct. We reject the ar-

F.C.C. No. 1, Transmittal No. 328, Pacific Bell Tariff F.C.C. No. 128, Transmittal No. 1738, US West Communications, Transmittal No. 550, *Memorandum Opinion and Order*, 10 FCC Rcd 1594 (Com. Car. Bur. 1994) (*Bell Atlantic/NYNEX Investigation Order*). The Bureau included the following four additional tariff filings in the investigation: Bell Atlantic Telephone Companies, Tariff F.C.C. No. 1, Transmittal No. 747, *Memorandum Opinion and Order Suspending Rates*, 10 FCC Rcd 5027 (Tariff Div. Com. Car. Bur. 1995); Pacific Bell, Tariff F.C.C. No. 128, Transmittal No. 1773 and US West, Tariff F.C.C. No. 5, Transmittal No. 584, *Memorandum Opinion and Order Suspending Rates*, 10 FCC Rcd 6038 (Tariff Div. Com. Car. Bur. 1995); The NYNEX Telephone Companies, Tariff F.C.C. No. 1, Transmittal No. 374, *Memorandum Opinion and Order Suspending Rates*, 10 FCC Rcd 8689 (Tariff Div. Com. Car. Bur. 1995).

<sup>23</sup> See 1993 Annual Access Tariff Filings, CC Dkt. No. 93-193, Phase I, CC Dkt. No. 94-65; AT&T Communications Tariff F.C.C. Nos. 1 and 2, Transmittal Nos. 5460, 5461, 5462 and 5464, CC Dkt. No. 93-193, Phase II; Bell Atlantic Telephone Companies Tariff F.C.C. No. 1, Transmittal No. 690, NYNEX Telephone Companies Tariff F.C.C. No. 1, Transmittal No. 328, CC Dkt. No. 94-157, *Order Designating Issues for Investigation*, DA 95-1485 (Com. Car. Bur., rel. June 30, 1995) (designating issues in three related investigations of claims for exogenous treatment of OPEBs amounts).

<sup>24</sup> Price Cap Performance Review for Local Exchange Carriers, *First Report and Order*, 10 FCC Rcd 8961, paras. 292-320 (1995).

<sup>25</sup> 1995 Annual Access Tariff Filings of Price Cap Carriers,

NYNEX Telephone Companies Tariff F.C.C. No. 1, Transmittal Nos. 379 and 384, New York Telephone Company Tariff F.C.C. No. 1152, Transmittal No. 1152, *Memorandum Opinion and Order Suspending Rates*, DA 95-1631 (Com. Car. Bur., rel. July 21, 1995) (*1995 Annual Access Order for Price Cap LECs*).

<sup>26</sup> 1995 Annual Access Tariff Filings of the NYNEX Telephone Companies and Pacific Bell, *Memorandum Opinion and Order on Reconsideration; Order Suspending and Investigating Rates*, CC Dkt. No. 94-157, DA 95-1665 (Com. Car. Bur., rel. July 27, 1995).

<sup>27</sup> *Id.*

<sup>28</sup> Net periodic costs include primarily benefits attributable to employee service during the current year and amortization of the transitional benefit obligation. Other elements of net periodic cost are interest costs, return on plan assets, amortization of unrecognized prior service costs, and gains and losses.

<sup>29</sup> 47 C.F.R. §32.5999(f).

<sup>30</sup> *Id.*

<sup>31</sup> 47 C.F.R. §32.5999(f)(2).

<sup>32</sup> Bell Atlantic Application for Review at 2-3.

<sup>33</sup> 47 C.F.R. §32.6728.

<sup>34</sup> Bell Atlantic Application for Review at 2.

<sup>35</sup> GTE Comments at 5; Pacific Telesis Comments at 2.

<sup>36</sup> Pacific Telesis Comments at 2-5 (citing 5 U.S.C. §553).

<sup>37</sup> GTE Comments at 2 & ii.

<sup>38</sup> NYNEX Comments at 3.

<sup>39</sup> *Id.*

gument that RAO 20 improperly changed the requirements of our Part 32 accounting rules. RAO 20 did not change those rules; it merely gave needed direction on handling the requirements of a new accounting standard under the existing rules in Part 32. Our Part 32 rules specifically provide for automatic adoption of GAAP standards to the extent possible consistent with regulatory needs. Under Section 32.16 of those rules,<sup>40</sup> carriers may adopt GAAP changes within 90 days of notifying the Commission of the change, unless the Commission notifies the carriers to the contrary.

16. The Part 32 accounts were designed to be sufficiently flexible that a rule change would not be necessary every time there was a change in GAAP. The accounts that RAO 20 directed carriers to use in implementing the accrual method of accounting for OPEB costs reflect this flexibility. For example, prepaid OPEB costs are noncurrent assets. Under Part 32, costs of this type are recorded in Accounts 1401 through 1410.<sup>41</sup> Account 1401 through 1408 provide for recording the specific costs defined by that account, and Account 1410 provides for recording all noncurrent assets that do not fall within Accounts 1401 through 1408. Because prepaid OPEB costs do not meet the definitions in Accounts 1401 through 1408, they are required to be recorded in Account 1410, as carriers were instructed in RAO 20. Similarly, the instructions for Account 4310 direct carriers to include in that account amounts accrued for such items as unfunded pensions and other long-term liabilities not provided for elsewhere in Part 32.<sup>42</sup> Unfunded OPEB liabilities fall into this category. Finally, the instructions for the expense matrix in Section 32.5999(f)(2) direct carriers to distribute payroll-related benefits such as pensions among the expense accounts in accordance with that matrix. Like pensions, OPEBs are a payroll-related benefit.<sup>43</sup> We thus find that because Part 32 already provides all the accounts necessary to record OPEB costs on an accrual basis, there was no need to change the Part 32 accounts to accommodate the GAAP method of accounting for OPEB costs.

17. Bell Atlantic asserts that Section 32.6728 of our rules<sup>44</sup> requires carriers to record cash payments made to retirees as an expense in Account 6728, Other general and administrative, and that RAO 20 changed this rule by improperly requiring carriers to record OPEB costs in additional expense accounts. We do not agree. Under the cash basis of accounting for OPEB costs used prior to SFAS-106, the costs to be recorded were paid on behalf of retired employees. Retired employees, by definition, are not employed by the company; therefore, cash payments made on their behalf cannot be related to payroll accounts. Thus, as required under Part 32, such payments had to be recorded as general and administrative expense in Account 6728 prior to the adoption of SFAS-106.

18. In contrast, OPEB costs recorded under the accrual method required by SFAS-106, for the most part, represent a benefit expense for current employees. Under Part 32, benefits for current employees must be recorded in the expense account categories used to record employees' payroll costs. Specifically, Section 32.5999(f)(2) requires that such expenses be recorded in the benefits subsidiary record category<sup>45</sup> of the functional account to which the employees' costs are assigned. The change to accrual accounting changed the nature of OPEB expenses recorded by the carriers -- these expenses now correspond to accrued amounts and not cash payments and they relate to current rather than retired employees. Thus, the provision in Account 6728 to record in that account the direct benefit payments to or on behalf of retired and separated employees no longer applied to these expenses.

19. Based on the above discussion we conclude that RAO 20 did not change the Part 32 accounting requirements; it merely interpreted them to give carriers the instructions they needed to implement SFAS-106. Because RAO 20 did not change any accounting requirements, there was no need to provide prior notice and an opportunity to comment, as Pacific Telesis contends.<sup>46</sup>

## B. RAO 20 Rate Base

### 1. Instructions

20. RAO 20 instructed the carriers to exclude the interstate portion of accrued liability related to OPEBs recorded in Account 4310 from their interstate rate base and to include the interstate portion of any prepaid OPEB benefits recorded in Account 1410 in that rate base. The basis for this instruction was the Bureau's belief that OPEB benefits were similar to pension benefits.<sup>47</sup> Because unfunded accrued pension costs are currently excluded from the rate base pursuant to Part 65 of our rules,<sup>48</sup> the Bureau concluded that accrued OPEB liability should receive similar rate base treatment.<sup>49</sup>

### 2. Pleadings

21. Bell Atlantic and NYNEX argue that an RAO letter cannot change the Commission's Part 65 rules defining a carrier's rate base. Bell Atlantic contends that, because those rules do not list OPEB costs as items to be excluded from the rate base, the portion of RAO 20 that directs carriers to exclude from the rate base unfunded OPEB costs recorded in Account 4310 is an impermissible change in the rules.<sup>50</sup> NYNEX states that Part 65 cannot properly be amended via an RAO letter.<sup>51</sup> The WUTC, while not asserting that RAO 20 violated the Commission's rules,

<sup>40</sup> 47 C.F.R. §32.16.

<sup>41</sup> 47 C.F.R. §§32.1401-1410. These accounts record costs for noncurrent assets associated with: (i) investments in affiliated companies; (ii) investments in nonaffiliated companies; (iii) nonregulated investments; (iv) unamortized debt issuance expense; and (v) sinking funds.

<sup>42</sup> 47 C.F.R. §32.4310.

<sup>43</sup> 47 C.F.R. §32.5999(f)(2).

<sup>44</sup> 47 C.F.R. §32.6728.

<sup>45</sup> Section 32.5999(f)(2) requires carriers to include payroll-related benefits on behalf of employees in the benefits subsidiary record category. OPEB benefits are earned as work is performed

and therefore they are payroll-related.

<sup>46</sup> See 5 U.S.C. §553(b)(3)(A) (Administrative Procedure Act notice and comment requirements not applicable to "interpretative rules").

<sup>47</sup> RAO 20, *supra* note 1, at 2872-73. Postretirement benefits are similar to pension benefits because they both are earned while the employee is working and they are paid to the employee, or on behalf of the employee, after retirement.

<sup>48</sup> 47 C.F.R. Part 65.

<sup>49</sup> RAO 20, *supra* note 1, at 2872-73.

<sup>50</sup> Bell Atlantic Application for Review at 2.

<sup>51</sup> NYNEX Comments at 6.

nonetheless urges the Commission to institute a rulemaking to consider more fully the rate base treatment of OPEB costs.<sup>52</sup>

22. Ameritech maintains that the rate base guidance set forth in RAO 20 should be deferred until the Commission determines whether these costs are exogenous under price cap regulation.<sup>53</sup> Ameritech rejects the notion that OPEB costs should necessarily be treated like pension costs. Ameritech states that the treatment of pension costs was decided at a time when rate of return regulation assured that any cost increases would be included in revenue requirements.<sup>54</sup> Because under price caps rates do not automatically increase when costs increase, Ameritech argues that, absent exogenous treatment of OPEB costs, the RAO 20 instructions governing rate base adjustments would be confiscatory. Ameritech states that any unfunded costs excluded from the rate base would constitute shareholder-supplied investment on which the shareholder would be entitled to earn a return.<sup>55</sup>

23. GTE and Pacific Telesis support Ameritech's position regarding exclusion of OPEB costs from the rate base. GTE states that any attempt to resolve this issue would be premature until there is a resolution of the underlying question of whether OPEB costs will be treated as exogenous.<sup>56</sup> Pacific Telesis contends that fundamental considerations of fairness require that the rate base issue be deferred until the issue of exogenous treatment of OPEB costs is resolved.<sup>57</sup> Pacific Telesis suggests that if the Commission denies exogenous treatment of OPEB costs, any unfunded OPEB costs should not be excluded from the rate base because they would not be ratepayer-supplied funds.<sup>58</sup>

24. NYNEX states that OPEB costs are similar to pension costs and thus should be afforded similar rate base treatment.<sup>59</sup> NYNEX contends that the exogenous treatment of OPEB costs should not be the driving force behind the rate base treatment of these costs.<sup>60</sup> In reply, however, Ameritech and Bell Atlantic argue that there is a necessary relationship between the question of the proper rate base treatment of OPEB costs and the question of whether such costs should be exogenous under price caps.<sup>61</sup>

### 3. Decision

25. After reviewing the record on this issue, we find that RAO 20 exceeded the Bureau's delegated authority to the extent that it directed exclusions from and additions to the rate base for which the Part 65 rules do not specifically provide. Sections 65.820 and 65.830 of our rules<sup>62</sup> define explicitly those items to be included in, or excluded from, the interstate rate base. The Bureau cannot properly address any additional exclusions in an RAO letter, which

under Section 32.17 of our rules<sup>63</sup> must be limited to explanation, interpretation, and resolution of accounting matters. Accordingly, the portion of RAO 20 that addresses the rate base treatment of prepayments and accrued liabilities related to OPEBs is rescinded.

## IV. PETITION FOR RECONSIDERATION

26. Bell Atlantic filed a Petition for Reconsideration of RAO 20 on June 3, 1992. Since this Order addresses the issues raised in that petition, we dismiss it as moot.

## V. NOTICE OF PROPOSED RULEMAKING

### A. Preliminary Matters

27. Today, we rescind that portion of RAO 20 addressing the rate base treatment of prepayments and accrued liabilities related to OPEBs.<sup>64</sup> In ordering such rescission, we base our action solely on procedural grounds, and render no decision on the substantive merits of the ratemaking practices at issue.<sup>65</sup> In this Notice of Proposed Rulemaking, we propose amendments to Part 65, Subpart G of our rules, to revise the rate base treatment of prepaid OPEB costs recorded in Account 1410, Other Noncurrent Assets, and all items in Account 4310, Other Long-Term Liabilities, including accrued liabilities related to OPEBs.

28. Several investigations of LEC tariffs that include exogenous adjustments for OPEB costs are pending.<sup>66</sup> The applicants and some commenters have suggested that we defer modifying our Part 65 regulations until the conclusion of these investigations.<sup>67</sup> Although we do not agree that we should delay our action proposing to modify Part 65 to require the exclusion from the rate base of all items in Account 4310, including accrued liabilities related to OPEBs, we invite comment on this issue.

29. RAO 20 instructed carriers to include in their rate bases the interstate portion of prepaid postretirement benefits recorded in Account 1410, Other Noncurrent Assets, and to remove from their rate bases the interstate portion of unfunded, accrued postretirement benefits recorded in Account 4310, Other Long-Term Liabilities.<sup>68</sup> The stated rationale for this treatment was that "postretirement benefits are similar to pension expenses . . . and as such should be given the same rate base treatment."<sup>69</sup> Under our current rules, unfunded accrued pension costs recorded in Account 4310 are removed from the rate base,<sup>70</sup> and prepaid pension costs in excess of the SFAS-87 periodic pension cost calculation recorded in Account 1410 are included in the rate base.<sup>71</sup> The FASB has commented on the similarity

<sup>52</sup> WUTC Comments at 7.

<sup>53</sup> Ameritech Application for Review at 2.

<sup>54</sup> *Id.* at 3.

<sup>55</sup> *Id.*

<sup>56</sup> GTE Comments at 4.

<sup>57</sup> Pacific Telesis Comments at 5-6.

<sup>58</sup> *Id.* at 6.

<sup>59</sup> NYNEX Comments at 4.

<sup>60</sup> *Id.* at 5.

<sup>61</sup> Ameritech Reply at 3-5; Bell Atlantic Reply at 2-3.

<sup>62</sup> 47 C.F.R. §§65.820, 65.830.

<sup>63</sup> 47 C.F.R. §32.17.

<sup>64</sup> See *supra* part III.B.3, para. 25.

<sup>65</sup> See *supra* part III.B.

<sup>66</sup> See discussion *supra* part II, paras. 8-10.

<sup>67</sup> See discussion *supra* part III.B.2, paras. 22-24.

<sup>68</sup> RAO 20, *supra* note 1, at 2873.

<sup>69</sup> *Id.* at 2872-73 (emphasis added).

<sup>70</sup> 47 C.F.R. §65.830(a)(3).

<sup>71</sup> See Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Report and Order*, 3 FCC Rcd 269, para. 43 & n.32 (1987) (citing Use of Certain Generally Accepted Accounting Principles in Part 32 of the Commission's Rules, *Memorandum Opinion and Order*, 2 FCC Rcd 6675 (1987) (discussing in paragraphs 14 and 15 the inclusion of prepaid pension costs exceeding the SFAS-87 cost calculations in the rate base)), *recon.*, *Order on Reconsideration*, 4 FCC Rcd 1697

between SFAS-106, Employers' Accounting for Postretirement Benefits Other Than Pensions, and pension accounting statements SFAS-87 and SFAS-88.<sup>72</sup> "[D]ifferent accounting treatment is prescribed [in SFAS-106] only when the [FASB] Board has concluded that there is a compelling reason for different treatment."<sup>73</sup> We tentatively agree with the conclusion in RAO 20 that the similarity between OPEB amounts and pension expenses recorded in Accounts 4310 and 1410 justifies this rate base treatment for OPEB amounts, as well as pension expenses, recorded in each of the accounts.

## B. Proposed Rule

### 1. Account 1410

30. At this time, under Section 65.820(c), amounts recorded in Account 1410 are included in the rate base "only to the extent that they have been specifically approved by this Commission for inclusion." SFAS-87 and SFAS-106 set forth standards for calculating the future pension and OPEB costs companies should accrue in the current period. When companies prepay these costs by, for example, paying amounts in excess of the current period expense into employee pension funds, they record these excess contributions in Account 1410. Under our current rules, with the rescission of the rate base portion of RAO 20, prepaid pension costs recorded in Account 1410 are included in the rate base,<sup>74</sup> but prepaid OPEB costs recorded in Account 1410 are not included in the rate base.<sup>75</sup> Both types of excess prepayments, however, produce returns that reduce the pension amounts companies must accrue in future periods. Because investors fund these excess prepayments, we propose to include both types of excess prepayments in the rate base. We invite comment on this proposal.

31. We have allowed prepaid pension costs to be included in the rate base, because pension fund prepayments in excess of the SFAS-87 cost calculation earn a return, which benefits the ratepayer by reducing later expenses.<sup>76</sup> The proposed modification to our rate base rules governing prepaid OPEB costs recorded in Account 1410 is premised

on our belief that the rationale underlying the rate base treatment of prepaid pension costs recorded in Account 1410 applies equally to prepaid OPEB costs recorded in that account. We invite comment on our tentative conclusion that prepaid OPEB costs in excess of the SFAS-106 cost calculation benefit the ratepayer and thus justify the inclusion of these prepayments recorded in Account 1410 in the rate base.

### 2. Account 4310

32. Under our current Part 65 rules, unfunded accrued pension costs recorded in Account 4310 are removed from the rate base,<sup>77</sup> although other items recorded in Account 4310, such as accrued OPEB liabilities, are not removed from the rate base. We propose amending our Part 65 rules to accord to all items in Account 4310 the same rate base treatment presently accorded unfunded accrued pension costs. We would modify Section 65.830(a), which enumerates specific items to be removed from the rate base, by broadening the current reference to the interstate portion of unfunded accrued pension costs in Section 65.830(a)(3) to include the interstate portion of all items in Account 4310. We also propose conforming amendments to Section 65.830(c), broadening the current reference to the interstate portion of unfunded accrued pension costs to include the interstate portion of all items in Account 4310. We invite comment on these proposals.

33. Our proposal to modify our rate base rules governing all Account 4310 liabilities is motivated by our continuing concern that zero-cost sources of funds, those funds provided to a carrier without cost to the investors, be removed from the rate base.<sup>78</sup> We believe that this proposal properly recognizes that ratepayers should only pay a return on those amounts that the carrier has prudently invested in used and useful plant. For example, accrued liabilities related to OPEBs are recorded in Account 4310. Where carriers have accrued OPEB costs, but have not paid their OPEB liability, the recovered but unpaid costs are capital available to the carrier at no cost. Consequently, the accrued OPEB liability recorded in Account 4310 should be removed from the rate base as a zero-cost source of funds.

(1989), *remanded sub nom. Illinois Bell Tel. Co. v. FCC*, 911 F.2d 776 (D.C. Cir. 1990), *on remand*, Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Decision on Remand*, 7 FCC Rcd 296 (1991), *aff'd sub nom. Illinois Bell Tel. Co. v. FCC*, 988 F.2d 1254 (D.C. Cir. 1993).

<sup>72</sup> SFAS-106, para. 11 n.6.

<sup>73</sup> *Id.* (discussing similarities in subheading "Similarity to Pension Accounting" in Summary and identifying major similarities and differences in Appendix B).

<sup>74</sup> See Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Report and Order*, 3 FCC Rcd 269, para. 43 & n.32 (1987) (citing Use of Certain Generally Accepted Accounting Principles in Part 32 of the Commission's Rules, *Memorandum Opinion and Order*, 2 FCC Rcd 6675 (1987) (discussing in paragraphs 14 and 15 the inclusion of prepaid pension costs exceeding the SFAS-87 cost calculations in the rate base)), *recon.*, *Order on Reconsideration*, 4 FCC Rcd 1697 (1989), *remanded sub nom. Illinois Bell Tel. Co. v. FCC*, 911 F.2d 776 (D.C. Cir. 1990), *on remand*, Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Decision on Remand*, 7 FCC Rcd 296 (1991), *aff'd sub nom. Illinois Bell Tel. Co. v. FCC*, 988 F.2d 1254 (D.C. Cir. 1993).

<sup>75</sup> 47 C.F.R. §65.820(c).

<sup>76</sup> See Use of Certain Generally Accepted Accounting Principles in Part 32 of the Commission's Rules, *Memorandum Opinion and Order*, 2 FCC Rcd 6675, paras. 14-15 (1987), *cited in* Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Report and Order*, 3 FCC Rcd 269, para. 43 (1987), *recon.*, *Order on Reconsideration*, 4 FCC Rcd 1697 (1989), *remanded sub nom. Illinois Bell Tel. Co. v. FCC*, 911 F.2d 776 (D.C. Cir. 1990), *on remand*, Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Decision on Remand*, 7 FCC Rcd 296 (1991), *aff'd sub nom. Illinois Bell Tel. Co. v. FCC*, 988 F.2d 1254 (D.C. Cir. 1993).

<sup>77</sup> 47 C.F.R. §65.830(a)(3).

<sup>78</sup> See generally Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Report and Order*, 3 FCC Rcd 269, paras. 51-61 (1987), *recon.*, *Order on Reconsideration*, 4 FCC Rcd 1697 (1989), *remanded sub nom. Illinois Bell Tel. Co. v. FCC*, 911 F.2d 776 (D.C. Cir. 1990), *on remand*, Amendment of Part 65 of the Commission's Rules to Prescribe Components of the Rate Base and Net Income of Dominant Carriers, *Decision on Remand*, 7 FCC Rcd 296 (1991), *aff'd sub nom. Illinois Bell Tel. Co. v. FCC*, 988 F.2d 1254 (D.C. Cir. 1993).

The same rationale could be applied to all items recorded in Account 4310, and we therefore wish to consider amending our rules to require that carriers exclude all Account 4310 items from their rate bases. In this rulemaking, we therefore undertake a comprehensive examination of the issues underlying the rate base treatment of long-term liabilities.

34. Under our proposals, we would require the removal from the rate base of all items recorded in Account 4310 because we believe that these amounts are zero-cost sources of funds. Account 4310 is a catch-all account, including "other long-term liabilities not provided for elsewhere."<sup>79</sup> Interest bearing liabilities, however, are not included in Account 4310.<sup>80</sup> We encourage parties to comment on the issue of whether all items recorded in Account 4310 are zero-cost sources of funds, which should be removed from the rate base. We also request comment on more modest amendments to Sections 65.830(a)(3) and 65.830(c) that would accord the same rate base treatment to accrued OPEB liabilities presently accorded unfunded accrued pension costs, without modifying the rate base treatment for other items in Account 4310.

### C. Procedural Matters

#### 1. Ex Parte

35. This is a non-restricted notice and comment rulemaking proceeding. Ex parte presentations are permitted, except during the Sunshine Agenda period, provided they are disclosed as provided in the Commission's rules.<sup>81</sup>

#### 2. Regulatory Flexibility

36. We certify that the Regulatory Flexibility Act of 1980 does not apply to this rulemaking proceeding because if the proposals in this proceeding are adopted, there will not be a significant economic impact on a substantial number of small business entities, as defined by Section 601(3) of the Regulatory Flexibility Act.<sup>82</sup> Because of the nature of local exchange and access service, the Commission has concluded that LECs, including small LECs, are dominant in their fields of operation and therefore are not "small entities" as defined by that act.<sup>83</sup> The Secretary shall send a copy of this Notice of Proposed Rulemaking, including the certification, to the Chief Counsel for Advocacy of the Small Business Administration in accordance with Section 603(a) of that act.<sup>84</sup>

#### 3. Comment Dates

37. We invite comment on the proposals and tentative conclusions set forth above. Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules,<sup>85</sup> interested parties may file comments on or before April 12, 1996, and reply comments on or before May 14, 1996. To file formally in this proceeding, you must file an original and four copies of all comments, reply comments, and supporting comments. If you want

each Commissioner to receive a personal copy of your comments, you must file an original plus nine copies. You should send comments and reply comments to Office of the Secretary, Federal Communications Commission, Washington, D.C. 20554. Parties should send one copy of any documents filed in this docket to the Commission's copy contractor, International Transcription Service (ITS), 2100 M Street, N.W., Suite 140, Washington, D.C. 20037. Comments and reply comments will be available for public inspection during regular business hours in the FCC Reference Center, Room 239, 1919 M Street, N.W., Washington, D.C. 20554.

### VI. ORDERING CLAUSES

38. Accordingly, IT IS ORDERED, pursuant to Sections 4(i), 201-205, and 220 of the Communications Act of 1934, 47 U.S.C. §§154(i), 201-205, 220, and Section 1.115(g) of the Commission's Rules, 47 C.F.R. §1.115(g), that the Applications for Review filed June 3, 1992, by the Ameritech Operating Companies and the Bell Atlantic Telephone Companies ARE GRANTED to the extent indicated above and ARE DENIED in all other respects.

39. IT IS FURTHER ORDERED, pursuant to Sections 4(i) of the Communications Act of 1934, 47 U.S.C. §154(i), that the Petition for Reconsideration filed June 3, 1992, by the Bell Atlantic Telephone Companies IS DISMISSED as moot.

40. Accordingly, IT IS ORDERED that, pursuant to Sections 1, 4(i), 4(j), 201 through 205, 220, and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 154(j), 201 through 205, 220 and 403, NOTICE IS HEREBY GIVEN of proposed amendments to Part 65, Subpart G of the Commission's Rules, 47 C.F.R. Part 65, Subpart G, as described in the Notice of Proposed Rulemaking.

### FEDERAL COMMUNICATIONS COMMISSION

William F. Caton  
Acting Secretary

<sup>79</sup> 47 C.F.R. §32.4310(a).

<sup>80</sup> Compare 47 C.F.R. §32.4310(a) (including in account 4310 "other long-term liabilities not provided for elsewhere") with §32.4270(a) (including in account 4270 "long-term debt not provided for elsewhere").

<sup>81</sup> See generally 47 C.F.R. §§ 1.1202, 1.1203, 1.1206(a).

<sup>82</sup> 5 U.S.C. § 601(3).

<sup>83</sup> See MTS and WATS Market Structure, Third Report and Order, 93 F.C.C.2d 241, para. 360 (1983).

<sup>84</sup> 5 U.S.C. § 603(a).

<sup>85</sup> 47 C.F.R. §§ 1.415, 1.419.